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Hugh Evander Willis

Indiana University School of Law - Bloomington

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CORPORATIONS AND THE UNITED STATES CONSTITUTION

HUGH EVANDER WILLIS

Professor of Law, Indiana University School of Law

The original United States Constitution is absolutely silent upon the subject of corporations. The young "fathers" of the Constitution apparently never gave the matter of corporations a thought. This is one of the great omissions of the original United States Constitution. Yet, by the United States Constitution, which has been made by the Supreme Court, corporations today are protected in most respects as much as natural persons, and in some respects, more than natural persons; although there are a few respects in which they are not yet protected to the same extent as natural persons, but perhaps this difference will disappear in the course of time. In the same way the liabilities of corporations have been worked out under and through the judge-made United States Constitution.

In the early history of our constitutional law, especially in the pronouncements of Chief Justice Taney, there obtained the restrictive or geographical theory of corporations, according to which a corporation could

have no legal existence outside of the boundaries of the state by which it was created. Under this theory it would have been difficult to have applied very many constitutional provisions to corporations. Yet the decisions of the United States Supreme Court have more and more extended the protection of the Constitution to corporations and have evolved the rules of the liability of corporations according to constitutional doctrines; so that, whether or not the Supreme Court admits it, it has finally in fact adopted a liberal theory as to the existence of a corporation. As a consequence, the jural relations between a state, or the United States, and a corporation are those existing under the functional or legal entity theory, according to which it may have a legal existence anywhere though incorporated only in one state by which it was created. Under this theory it constitutional provisions should not apply to a corporation the same as to a natural person. This article will be concerned with the questions of the status of corporations under the real present United States Constitution, and of the extent to which the power of reason has prevailed over the power of ritual.

I.

PROTECTION: 1. AS CITIZENS

To what extent are corporations protected by the United States Constitution as citizens? Corporations are not citizens of the United States under the definition of a citizen in Section 1 of the Fourteenth Amendment to the Constitution,¹ and probably for this reason are

¹Bankers Trust Co. v. Texas and P. R. Co., 241 U. S. 295 (1916); Insurance Company v. New Orleans, Fed Cas. No. 7052 (1870).

not protected by the clause as to abridging the privileges or immunities of citizens of the United States.'

Corporations are not citizens of any state within the meaning of Section 2, Article IV, of the United States Constitution, so as to be entitled, in other states than their creation, to all the privileges and immunities which such states give to their own citizens.' For this reason, a state may still prescribe the conditions on which a foreign corporation may do business within its border or exclude it altogether,' unless such foreign corporation is engaged in interstate commerce or is in the employ of the federal government.'

But a corporation is now a citizen of the state of its creation for the purpose of federal jurisdiction on the ground of diversity of citizenship.' The genesis of this doctrine is interesting. At first, a corporation was not regarded as a citizen for any purpose and it could not get into or be taken into the federal courts on the ground of diversity of citizenship.' Then a case arose where all

**Terrell v. Burke Construction Co.*, 257 U. S. 529 (1922), held that a state had no power to impose on a foreign corporation a condition that it would not sue in the federal courts, because such corporation had the privilege of suing in the federal courts. This decision can be rationalized only by holding either that thereby a foreign corporation is made a citizen of the United States under the Fourteenth Amendment; or that though it is not such a citizen, it is a citizen for the purpose of suing in the federal courts under Section 2 of Article 3 of the United States Constitution, and that therefore, a state would be violating our doctrine of a dual form of government to interfere thus with the jurisdiction of the federal courts. The last explanation is probably the true explanation.

**Western Turf Association v. Greenberg*, 204 U. S. 359 (1907); *Blake v. McClung*, 172 U. S. 239 (1898); *Paul v. Virginia*, 8 Wall. 168 (1869).

**Blake v. McClung*, 172 U. S. 239 (1898); *Paul v. Virginia*, 8 Wall. 168 (1869); *Hammond Packing Co. v. Arkansas*, 212 U. S. 29 (1909).

**Pensacola Tel. Co. v. Western Union Tel. Co.*, 96 U. S. 1 (1878); *Horn Silver Mining Co. v. New York*, 143 U. S. 305 (1892).

**Nashua and L. R. Corp. v. Boston and L. R. Corp.*, 136 U. S. 356 (1890).

*2 WILLoughBY, *THE CONSTITUTION OF THE UNITED STATES* (1929) p. 1291.

of the stockholders of the corporation were citizens of the same state where the corporation was incorporated and the plaintiff was a citizen of another state, and it was held that the court would look behind the corporate veil to the stockholders and give the federal courts jurisdiction because of the diversity of citizenship thus found.⁹ In a later case, some of the stockholders were not citizens of the state where the corporation was incorporated, but of the state in which the opposing litigant was a citizen. To avoid robbing the federal courts of their jurisdiction, the Court held that for purposes of diversity of citizenship all of the stockholders of a corporation would be conclusively presumed to be citizens of the chartering state.¹⁰ This rule, however, had to be modified later so as to make an exception in the case of a stockholder plaintiff.¹¹ Now it is believed that the courts have come to the position that the corporation is itself a citizen of the state of its incorporation for the purposes of diversity of citizenship.¹²

However, it should be noted that a state apparently has the power of destroying federal jurisdiction over foreign corporations because of diversity of citizenship, and the privilege of foreign corporations to sue in the federal courts, by requiring incorporation in such state

⁹Bank of the United States v. Deveaux, 5 Cranch 61 (1809).

¹⁰Marshall v. B. & O. R. R. Co., 16 How. 314 (1853).

¹¹Doctor v. Harrington, 196 U. S. 579 (1905).

¹²St. Louis v. James, 161 U. S. 545 (1896); Doctor v. Harrington, 196 U. S. 579 (1905). This was so held first in the case of Louisville R. R. Co. v. Letson, 2 How. 497 (1844), and Rundle v. Canal Co., 14 How. 90 (1852); but for fear that these cases made a corporation a citizen under all the citizenship clauses, they were modified by the case of Marshall v. B. & O. R. R. Co., 16 How. 314 (1853), and the residence fiction of the stockholders relied upon, but the inadequacy of this explanation has forced the courts to regard a corporation as a citizen to this extent; and probably Terrell v. Burke Construction Co., 257 U. S. 529 (1922), goes no further than this. See also Burnet v. Commonwealth, 53 Sup. Ct. 198 (1932).

before it will allow the corporation to do business therein. In such case, the corporation would be a new corporation and a citizen of such state so that it would not have the privilege of suing in the federal courts as against the citizens of that state."¹¹

Warren is of the opinion that the framers of the judiciary act did not contemplate the diversity clause should apply to corporations. At first the corporations themselves did not want the advantage of the diversity clause and they escaped federal jurisdiction if any stockholder was a citizen of a state with the plaintiff. Yet little by little as shown hereafter the jurisdiction of the federal courts was upheld as applying to corporations. The reasons given were local prejudice and the need of inducing capital in the south and west. The present reasons why corporations prefer federal jurisdiction to state are to get a different substantive law and to get a different kind of court. It is clearly true that the reasons for diversity of citizenship jurisdiction apply with special force to corporations. Corporations have unlimited power to influence state courts and they are generally concerned with matters of a commercial nature where there is a need for uniform law."¹²

Corporations may have been given too much protection in some respects to be referred to hereafter, but there are some respects in which they have not been given protection enough, and the writer submits that protection as a citizen is one. The Supreme Court has made a great deal of constitutional law for corporations in the matter of citizenship, but it has not yet made enough. The discriminations of the various states

¹¹*Railway Express Agency v. Virginia*, 282 U. S. 440 (1931).

¹²Warren, *Corporations and Diversity of Citizenship*, 19 VA. L. REV. 661 (1933).

against foreign corporations not engaged in interstate commerce or in the employ of the federal government, especially in the matter of taxation, are so unfair as to be almost scandalous. Why, simply because they happen to be incorporated in a sister state, should one state be allowed to extort of foreign corporations levies which it does not exact from domestic corporations? The Constitution does not permit it to do such a thing in case of natural persons. It would seem that every argument for one should apply to the other. Natural persons are protected by the interstate (rights) privileges and immunities clause of Article IV, Section 20, and corporations should receive this same protection. All it would be necessary to do to accomplish this result would be for the Supreme Court to declare that corporations are citizens for this protection. This step would be much shorter than other steps it has taken, and would seem to be the natural culmination of what it has already done.

PROTECTION: 2. AS PERSONS

To what extent are corporations protected as persons under the United States Constitution? The answer to this question is that they as to their property have as full and complete protection as natural persons. Corporations are persons, though they are artificial persons, but they are just as real entities as natural persons. At first, the protection of the due process clause and the equality clause of the Fourteenth Amendment was extended only to negroes." Then the protection of these clauses was extended to the protection of natural persons, first, as to procedure," and then as to matters

¹¹Slaughter House Cases, 16 Wall. 36 (1873).

¹²Munn v. Illinois, 94 U. S. 113 (1876).

of substance," and finally, largely through the influence of Justice Field, their protection was extended to the property rights of corporations."

It is true the protection of the equality clause extends only to persons "within" the jurisdiction of a state, and a corporation not engaged in interstate commerce or in the employ of the federal government would be subject to the power of the state in getting into the state or staying in the state, so that the protection of the equality clause would mean very little." But recently, in the case of *Kentucky Finance Corporation v. Paramount Automobile Company*," the Supreme Court seemed to extend the protection of the equality clause to the protection of a foreign corporation in the matter of suit in a state court, even though not within the jurisdiction of a state. In this case, the Supreme Court held that a Kentucky corporation could go into Wisconsin and sue to replevin an automobile without submitting to examination as required by a statute applying only to foreign corporations. But apparently the Wisconsin law permitted foreign corporations to sue in its courts, so that it might be contended that the corporation was within the state and therefore entitled to the protection of the equality clause. Yet, the language of the court is broad enough to support the proposition that a state may not bar a foreign corporation from legitimate resort to its courts."

The due process clause has been invoked to protect corporations against taxation, except at their situs, both

¹¹Davidson v. New Orleans, 96 U. S. 97 (1878).

¹²Minneapolis v. Beckwith, 129 U. S. 26 (1889); Covington v. Sandford, 164 U. S. 578 (1896).

¹³Blake v. McClung, 172 U. S. 239 (1898).

¹⁴262 U. S. 544 (1923).

¹⁵79 U. OF PA. L. REV., 962-4 (1931).

as to general property taxes¹⁰ and inheritance taxes¹¹ on land and tangible chattels, unless under the unit rule,¹² or unless the tangible chattels have no situs;¹³ and on intangible chattels, unless they have acquired a business situs, except at the domicile of the owner (creditor) which in the case of a corporation is the state of incorporation,¹⁴ and this rule applies though the intangibles are evidenced by tangibles.¹⁵ It thus protects corporations against multi-taxation by different states. The due process clause also protects corporations as much as natural persons against the taking of their property by eminent domain¹⁶ or by the police power.¹⁷ Public utilities especially have received protection as to their rates of return and rate bases.

A corporation has been protected as a person in many other incidental ways. Thus, it has been given the right as a person to file a mechanic's lien,¹⁸ to obtain the protection of bankruptcy laws,¹⁹ and to petition to quiet title.²⁰

Corporations are protected by the provision of Section 10, Article I, of the United States Constitution against laws impairing the obligation of contracts. In the

¹⁰Union Refrig. Tr. Co. v. Kentucky, 199 U. S. 194 (1905).

¹¹Frick v. Pennsylvania, 268 U. S. 473 (1925).

¹²New York, etc. v. Miller, 202 U. S. 584 (1906).

¹³Southern Pacific Co. v. Kentucky, 222 U. S. 63 (1911).

¹⁴Farmers L. & T. Co. v. Minnesota, 280 U. S. 204 (1931); Rhode Island Hospital Trust Co. v. Doughton, 270 U. S. 69 (1926).

¹⁵Beidler v. South Carolina, 282 U. S. 1 (1930).

¹⁶State ex rel. Tacoma Ice Co. v. White River Power Co., 39 Wash. 648, 82 Pac. 150 (1905); Long Island W. Sup. Co. v. Brooklyn, 166 U. S. 685 (1897).

¹⁷Reagen v. Farmers Loan & Trust Co., 154 U. S. 362 (1894).

¹⁸Chatman v. Brewer, 43 Neb. 890, 62 N. W. 320 (1895).

¹⁹Barth v. Bachus, 140 N. Y. 230, 35 N. E. 425 (1893).

²⁰Proprietors v. Inhabitants of Ipswich, 153 Mass. 42, 26 N. E. 239 (1891).

Dartmouth College Case," the United States Supreme Court held that a corporate charter was a contract entitled to such protection. Subsequent cases interpreted this protection to mean that such charters were not subject to the state's subsequent exercise of its police power, or power of taxation, or perhaps even of eminent domain." This was giving corporations greater protection than has ever been given natural persons, and is largely responsible for the great development of the corporation method of business organization in the United States, which has finally resulted in making our civilization a corporate civilization. It is true that the Supreme Court finally made the protection of corporate charters subject to the exercise of the power of eminent domain," and to the exercise of the police power," except in the case of rates of public utilities;" but it is still held that corporate charters are not subject to the exercise of the police power in the matter of rates of public utilities and in the matter of taxation."

Corporations are protected as much as natural persons against unreasonable searches and seizures."

Corporations are not protected by the constitutional guaranty against self-crimination, on the theory that the constitutional protection was not intended for those

¹¹⁴Wheat, 518 (1819).

¹¹⁵Bridge Proprietors v. Hoboken Co., 1 Wall. 116 (1864); Piqua Bank v. Knoop, 16 How. 369 (1853).

¹¹⁶Long Island Water Co. v. Brooklyn, 166 U. S. 685 (1897); West River Bridge Co. v. Dix, 6 How. 507 (1848).

¹¹⁷Stone v. Mississippi, 101 U. S. 814 (1880); Illinois Central Ry. Co. v. Illinois, 146 U. S. 387 (1892).

¹¹⁸Columbus Ry., Power & Light Co. v. Columbus, 249 U. S. 399 (1919).

¹¹⁹Lake Superior Consolidated Iron Mines v. Lord, 271 U. S. 577 (1926); Roberts & Schaefer Co. v. Emmerson, 271 U. S. 50 (1926).

¹²⁰Hale v. Henkle, 201 U. S. 43 (1906).

who could not be punished criminally." But now that corporations are becoming more and more amenable to criminal law, it may be argued that the rule should be changed."

Is a corporation entitled to a jury trial in either a criminal case or a civil case? It would seem that a corporation should be entitled to the right to a jury trial in both civil and criminal cases, but the question might be a little more difficult in a criminal case."

The power of eminent domain is inherent in sovereignty. Constitutional recognition of its existence is unnecessary. It is also implied that the exercise of this sovereign power is delegated to the state. Express delegation is unnecessary." Yet this sovereign power may in turn be delegated by the state either to other governmental subdivisions or to private corporations, provided the exercise of the power involves the taking of property for a public use only. Corporations engaged in businesses affected with a public interest (public callings) are performing such a governmental function that the taking of property for their own uses is a public use and therefore constitutional."

The commerce clause protects corporations as natural persons against taxation by the states for the privilege

"Wilson v. United States, 221 U. S. 361 (1911).

"Silverthorn v. United States, 251 U. S. 385 (1920); 27 MICH. L. REV. 471 (1929).

"State v. Standard Oil Co. of Kentucky, 120 Tenn. 86, 110 S. W. 565 (1908).

"United States v. Jones, 109 U. S. 513 (1883); People v. Adirondack Ry. Co., 160 N. Y. 225, 54 N. E. 689 (1899).

"Varner v. Martin, 21 W. Va. 534 (1883); *In re* Niagara Falls & W. Ry. Co., 108 N. Y. 375, 15 N. E. 429 (1888); Nolan v. Central Ga. Power Co., 134 Ga. 201, 67 S. E. 656 (1910); Evergreen Cemetery Association v. Beecher, 53 Conn. 551, 5 Atl. 353 (1885).

of doing interstate commerce," although they are subject to non-discriminatory property taxes;" and license taxes for use of highways and other privileges;" and against the exercise of the police power of the states over interstate commerce where the federal government's power is exclusive," except where it is the states' general police power and not a direct regulation of interstate commerce."

The commerce clause protects corporations engaged in interstate commerce, although not natural persons and other corporations, against suit in a state other than its incorporation on a transitory cause of action which has arisen in another state, because the Supreme Court has said this is a burden on interstate commerce." It would seem that it would have been better for the Supreme Court to have rested its decision on the denial of due process. Then all corporations, and also natural persons, would have been protected.

The commerce clause also guarantees the right to sue in a state court on interstate business done in that state without complying with state restrictions as to appointment of a resident agent or filing of a charter."

Corporations as persons are protected as much as

"Case of State Freight Tax, 15 Wall. 232 (1872); *McCall v. California*, 136 U. S. 104 (1890).

"*Gloucester Ferry Co. v. Pennsylvania*, 114 U. S. 196 (1885); *St. Louis v. Nattin*, 277 U. S. 157 (1928).

"*Pocket Co. v. Keokuk*, 95 U. S. 80 (1873); *Huse v. Glover*, 119 U. S. 543 (1886); *Kane v. New Jersey*, 242 U. S. 160 (1916).

"*Pensacola Tel. Co. v. Western Union Tel. Co.*, 96 U. S. 1 (1878); *Buck v. Kuykendall*, 267 U. S. 307 (1925); *Commonwealth v. Attleboro*, 273 U. S. 83 (1927).

"*Smith v. St. Louis and S. W. Ry.*, 181 U. S. 248 (1901); *Sherlock v. Alling*, 93 U. S. 99 (1876).

"*Davis v. Farmers Co-Operative Equity Co.*, 262 U. S. 312 (1923); *Denver v. Terte*, 52 Sup. Ct. 152 (1932).

"*Sioux Remedy Co. v. Cope*, 235 U. S. 197 (1914).

natural persons by the constitutional guaranty of freedom of speech and the press, as is shown by the following cases where the courts hold that the constitutional guaranty does not apply because of exceptions to the rule."

Corporations as persons are protected as much as natural persons by the constitutional guaranty against double jeopardy."

As a result of all the protection given to corporations by the United States Constitution the growth of corporations in the United States has been nothing less than marvelous.

Before 1800 there were only 335 profit seeking corporations; 219 of these were turnpike, bridge and canal corporations; 67 of these were banking and insurance corporations; 36 of these were water and fire protection corporations; only 6 were manufacturing corporations.

In 1813 there was organized the Boston Manufacturing Company concerned with textiles. This corporation introduced many of the present characteristics of corporations. But the growth of corporations in the textile industry stood still after the conclusion of the Civil War so that today the textile industry has not become quasi public in the sense that the public generally is the owner of the stock.

There was great development among railroads in the

⁸⁰Mutual Film Corp. v. Ohio Industrial Commission, 215 Fed. 138 (D. C. Ohio, 1914; Same, 236 U. S. 230 (1915) (not press); United States v. Toledo Newspaper Co., 220 Fed. 458 (D. C. Ohio, 1915); Same, 237 Fed. 986 (C. C. A. 6th, 1916) (contempt); Mutual Film Corp. v. Chicago, 224 Fed. 101 (C. C. A. 7th, 1915) (films); Deiner v. Star-Chronicle Pub. Co., 230 Mo. 613, 132 S. W. 1143 (1910) (libel); Kelley v. Independent Pub. Co., 45 Mont. 127, 122 Pac. 735 (1912) (libel); Williams Printing Co. v. Saunders, 113 Va. 156, 73 S. E. 472 (1912) (libel).

⁸¹Commonwealth v. Standard Oil Co., 120 Ky. 724, 90 S. W. 233 (1905); State v. Shevlin-Carpenter Co., 99 Minn. 158, 108 N. W. 935 (1906).

ante-bellum period. The New York Central Railroad was created in 1853 by the grouping of various railroads. Since the Civil War quasi public corporations have dominated the field of the rails. In 1930, 14 of these systems operated 81 per cent. of all the mileage in the United States.

Other aspects of our economic life have come under the sway of the corporation. This is almost universally true in banking, insurance and utilities. In mining and quarrying 93 per cent. of the business was conducted by corporations in 1919. In manufacturing 66 per cent. of the business was conducted by corporations in 1899; 87 per cent. in 1919 and 94 per cent. in 1933. The sway of the corporation has been delayed in certain other aspects of our economic life so that in clothing only 54 per cent. of the industry is dominated by corporations, in bread and baking only 51 per cent., in millinery only 46 per cent., in automobile repairing only 39 per cent. In mercantile business in general the corporation is just beginning to dominate. In 1909 the corporation dominated only 30 per cent. of the wholesale business and 15 per cent. of the retail business, but in 1925 it dominated 40 per cent. of the wholesale business and 30 per cent. of the retail. Forty to 60 per cent. of the construction work is done by corporations. Much of our real estate is held by corporations. In the case of municipal corporations operation is by managers but, outside of such corporations as the Port of New York Authority and the Tennessee Valley Authority, stock ownership is not widely dispersed. But corporations have made the least headway in agriculture where they dominate only 4 per cent. of the enterprise.

Enough figures have been given to show how completely our economic life has become dominated by

corporations. Corporations have now gathered property under their system. Corporations control the production and the distribution of products, and almost all other aspects of our economic life so that our civilization has in a real sense become a corporate civilization.

The evolution of the corporate structure also has been almost startling.

In England in the eighteenth century a corporation was a franchise, that is, a privilege granted with the grant of other privileges. The main characteristic of the corporation at this time was the limited liability of stockholders. In the beginning the charter of the corporation embodied all of the arrangements and was a contract between the corporation and the state (though there was no corporation yet), between the stockholders and the corporation, and between the stockholders *inter se*.

In the United States in the early nineteenth century it was customary to grant special charters to corporations. Under these, corporations were state controlled and there was a real agreement between the parties. This agreement undertook to protect the interest of the public, the interest of the creditor, and the interest of shareholders. By statute, limitations were imposed upon the scope of management, for the protection of the public and the shareholders; upon the supervision of payment for stock, so that no one would share in the profits unless he contributed to the original funds, so as to protect the creditors and the shareholders; and upon the capital structure set up. By the common law at this time control was in the shareholders. They had pre-emptive rights, dividends were paid only out of surpluses and while the corporation could be changed by

contract the contract had to be supervised by the state. Management was a set of agents running the business for a set of owners and accountable to them.

Beginning with the general incorporation laws of 1837 in Connecticut and running to the end of the nineteenth century corporations were allowed to engage in any lawful business. Large scale production was introduced and the growth in the number of shareholders began. With the introduction of this method of incorporation the legislature was eliminated and only the Secretary of State appeared for the government. While charters were still called contracts they were drafted solely by the incorporators or their attorneys and were buried with the Secretary of State. No one, save the clerks and the incorporators, knew their contents. The rigid requirements for the protection of the various parties interested in the corporation were broken down. As a consequence many new and little understood characteristics were introduced into the corporate structure.

One of these characteristics was the weakening of control by the stockholders over the direction of the enterprise. This was brought about through the use of proxies, through the limitation of the right to remove directors during their term, through the provision of amendment by a two-thirds majority, through the delegating of powers to voting trusts, through non-voting stock, and through the sale of property.

Another characteristic was the elimination of state supervision over the contributions of capital. With this lack of supervision property as well as cash was paid for stock and non-par stock was issued.

Another characteristic was the diminution of the right to invest additional monies. Pre-emptive rights were

eliminated if more shares were authorized in the original charter, or if stock was issued for property, or if the right was waived in the charter (as in many Delaware corporations).

Another characteristic was the modification of the restrictions on dividends. One device to accomplish the purpose of issuing dividends was through "paid in surpluses" in over-par and non-par stock. Delaware laws permit dividends though there are no profits.

Another characteristic was the elimination of the right to a fixed capital structure and a fixed place therein, by an insertion in the charter of the power to amend either by state authority or by action of majority against others.

Another characteristic was the limitation of the right in the future of the enterprise. This was brought to pass through the use of "stock purchase warrants" (a Delaware device), option, or unissued stock of fixed price.

In addition the inside group in corporations has acquired the power to route the earnings. In the case of non-cumulative preferred no dividends can be declared. In class A and class B stock the inside group can increase the stock of one class so that others can get more earnings and can use the surplus to buy in one class of stock. In the case of stock dividends they can declare a dividend to common stock, for example. They also can take advantage of stock purchase warrants, already referred to, can control the accounting, and can control earnings through the pyramiding of holding companies. All of these materially affect the owners of the corporation. As a consequence shareholders have surrendered a set of definite rights for a

set of indefinite expectations which normally cannot be enforced.

The inside group also has the power to affect creditors. This they can do through a power to alter the original contract either by amendment or merger. The contract between the shareholders and the corporation is not affected by the reserve power of the state. Therefore, it is a proper exercise of the police power for the state itself to make such changes or to confer the power on the majority."^a

II.

LIABILITY: 1. CORPORATIONS ENGAGED IN INTERSTATE COMMERCE

The Constitution of the Constitutional Convention does not expressly give the federal government the power to tax interstate commerce, but this power would undoubtedly be implied, although as yet the federal government has not tried to exercise this power. In the same way this Constitution does not expressly deny the power of taxation to the various state governments, but the Supreme Court has written into our Constitution a limitation that the state governments cannot tax interstate commerce, evidently on the theory that it would interfere with the federal government's regulation of interstate commerce." Hence, as we have seen above, a state cannot impose a tax on a foreign corporation engaged in interstate commerce for the privilege of doing interstate commerce." But a state may tax a foreign corporation for the privilege of doing local

^a"BERLE AND MEANS, *THE MODERN CORPORATION AND PRIVATE PROPERTY* (1933).

^bCase of State Freight Tax, 15 Wall. 232 (1873).

^cPensacola v. Western Union Tel. Co., 96 U. S. 1 (1878).

business, even though it is also engaged in interstate commerce, provided it does not base its fee on the total authorized capital stock of the corporation or otherwise burden interstate commerce;" and a state may levy an excise tax on a corporation engaged in interstate commerce for the privilege of using the state's highways;" and the Supreme Court now permits a state to levy a non-discriminatory property tax upon all the land" and tangible chattels" of a corporation located within the state, and on goods carried even though still in the original package, if they have become a part of the general mass of property of the state," though not upon intangibles unless the corporation is chartered by such state;" although under the unit rule, a state may tax a proportion both of tangibles and intangibles." A state may also levy a gross receipts tax in lieu of property taxes;" and after interstate commerce has ended and intrastate commerce begun, the state can, of course, levy property taxes."

While a state cannot levy an excise tax on a corporation whose business is wholly interstate," and perhaps not an income tax unless on the ground of citizenship," yet if the corporation is within the state the latter can

¹⁴East Ohio Co. v. Ohio Tax Commission, 283 U. S. 465 (1931); Cudahay v. Henkle, 278 U. S. 460 (1929).

¹⁵New Jersey Bell Tel. Co. v. State Board of Taxes, 280 U. S. 338 (1930).

¹⁶Gloucester Ferry Co. v. Pennsylvania, 114 U. S. 196 (1885).

¹⁷Pullman's Palace Car Co. v. Pennsylvania, 141 U. S. 18 (1891).

¹⁸Brown v. Houston, 114 U. S. 622 (1885). Import cases *contra*: Anglo Chilean Nitrate Sales Corp. v. Alabama, 53 Sup. Ct. 373 (1933).

¹⁹Baldwin v. Missouri, 281 U. S. 586 (1930).

²⁰Adams Express Co. v. Ohio State Auditor, 166 U. S. 185 (1897).

²¹United States Express Co. v. Minnesota, 223 U. S. 335 (1912).

²²77 U. OF PA. L. REV. 918 (1929).

²³Alpha Portland Cement Co. v. Massachusetts, 268 U. S. 203 (1925).

²⁴Cook v. Tait, 265 U. S. 47 (1924); Lawrence v. State Tax Commission, 286 U. S. 276 (1932).

probably levy an excise tax for the privilege of doing state business even if there is no income attributable to the state." A state may levy an income tax on a foreign corporation engaged in interstate commerce if it relies on some sort of allocation formula whereby it segregates the income from within the state from that without the state, as, for example, such part of the corporation's income as is represented by the proportion between the taxable property within the state and the total property of the corporation," if reasonable," and for purposes of taxation a corporation and its stockholders are clearly held to be separate entities."

The federal government has a complete police power over corporations engaged in interstate commerce," and under this power the federal government may also regulate intrastate commerce where intrastate and interstate commerce are so united that it is necessary to regulate both in order to regulate interstate commerce." But in spite of the federal government's power, the Supreme Court has held that the various state governments have a concurrent police power in the absence of federal action where the matter is not national in scope," and even where the federal government's power is exclusive, it has held that the state governments have

"Hump Hairpin Co. v. Emmerson, 258 U. S. 290 (1922); Detroit International Bridge Co. v. Corporation Tax Appeal Board of Michigan, 53 Sup. Ct. 137 (1932).

"Underwood Typewriter Co. v. Chamberlain, 254 U. S. 113 (1920); Bass, Ratcliff & Gretton, Ltd. v. State Tax Commission, 266 U. S. 271 (1924).

"Hans Rees' Sons, Inc. v. North Carolina, 283 U. S. 123 (1931).

"Burnet v. Commonwealth, 53 Sup. Ct. 198 (1932); Dalton v. Bowers, 53 Sup. Ct. 205 (1932).

"HUGHES, THE SUPREME COURT OF THE UNITED STATES (1928) p. 137.

"Shreveport Case, 234 U. S. 342 (1914); Georgia Public Service Commission v. United States, 283 U. S. 765 (1913).

"Cooley v. Board of Port Wardens, 12 How. 299 (1851).

an incidental or indirect power of regulation." But the Supreme Court has held that it is a burden on interstate commerce for a state court to take jurisdiction of a transitory cause of action against a non-resident corporation not doing business in the state," or to require appointment of a resident agent or filing of charter as conditions precedent to suing in its courts."

LIABILITY: 2. FOREIGN CORPORATIONS NOT ENGAGED IN INTERSTATE COMMERCE

A foreign corporation not engaged in interstate commerce may be taxed by the states through excise taxes practically at their whim, unless the corporation is within the taxing state, since in that case it is not entitled to the protection of the equality clause," and even as to corporations within the state it is generally a proper classification to tax corporations and no one else, or to tax certain corporations and not other corporations."

Except where intrastate commerce is bound up with interstate commerce, a state has a full and complete police power over all foreign corporations within its jurisdiction, except that it must not deny the corporation due process of law" and the privilege of suing in the federal courts." It may prescribe any condition it chooses as a condition to giving a corporation the privilege of doing business in the state," with the possible

⁷²Public Utilities Commission v. Attleboro Co., 273 U. S. 83 (1927).

⁷³Davis v. Farmers Co-operative Equity Co., 262 U. S. 312 (1923).

⁷⁴Sioux Remedy Co. v. Cope, 235 U. S. 197 (1914).

⁷⁵Blake v. McClung, 172 U. S. 239 (1898).

⁷⁶State Board of Indiana v. Jackson, 283 U. S. 527 (1931).

⁷⁷Covington v. Sandford, 164 U. S. 578 (1896).

⁷⁸Terral v. Burke Construction Co., 257 U. S. 529 (1922).

⁷⁹Wuchter v. Pizzutti, 276 U. S. 13 (1928).

exception of the privilege of suing in its courts," or the federal courts." But even if it could not impose these conditions directly, it could accomplish the same result by requiring a foreign corporation to incorporate in the state as a condition precedent to doing business in the state."

Foreign corporations are not protected by the contract clause against tax or other action by other states unless they have made new contracts with such states as by permission to do business therein under their exiting laws." Bankruptcy laws, though they override provisions in contracts, are apparently not inhibited by the contract clause or by the due process clause."

It was held at first that a state could acquire no jurisdiction over a foreign corporation, even though it was doing business within the state, since there was no possibility of service on it. This position was a two-fold result both of the doctrine of jurisdiction and of the concept of a corporation. The original Anglo-

"Kentucky Finance Corp. v. Paramount Auto. Corp., 262 U. S. 544 (1923).

"Terral v. Burke Construction Co., 257 U. S. 529 (1922).

"Railway Express Agency v. Virginia, 282 U. S. 440 (1931).

"American Smelting and Refining Co. v. Colorado, 204 U. S. 103 (1907).

"Canada So. R. R. Co. v. Gebhard, 109 U. S. 527, 536 (1883); *In re* Franklin Brewery Co., 249 Fed. 333 (C. C. A. 2nd, 1918); *Ogden v. Saunders*, 12 Wheat. 213 (1827); did not see that a subsequent state bankruptcy law might possibly be a proper exercise of the police power, but the above cases seem to uphold a subsequent federal bankruptcy law on this theory since, though the federal government is not limited by a contract clause, due process protects against the impairment of the obligation of a contract, *United States v. Northern Pacific Railway Co.*, 256 U. S. 51 (1921), and therefore limits the power of the federal government as much as the contract clause limits the power of the states. *Legal Tender Cases*, 12 Wall. 457 (1870); *Atlantic Coast Line v. City of Goldsboro*, 232 U. S. 548 (1913). If this is true, the same thing should be true of state moratoriums on the period of redemption of mortgages and bank deposit withdrawals, but former state stay laws have generally been declared unconstitutional unless making only slight changes in remedies. 27 ILL. L. REV. 799 (1933).

American notion of jurisdiction was that of the physical power which the court had, if need be, to lay the defendant by the heels. This required actual physical presence." The original notion of a corporation was that it was a metaphysical entity and could have legal existence only within the state of its creation. Hence, it could not be physically present in any other state so as to give such state jurisdiction over it. The law of private corporations is an outgrowth of the law of municipal corporations. Of course, a municipal corporation could not migrate, and the courts, therefore, at first took the position that a private corporation could not migrate."

The results of such a holding as the above were very unfortunate. A corporation could be sued only in the state where it was incorporated. This involved expense of travel and difficulty of getting witnesses, as well as the necessity of suing on a judgment where the corporation had no property in the state of its incorporation. In some cases, where the suit was local in character, there could be no relief. Consequently, the states, by statute, undertook to change the situation so as to make corporations liable to suit in the state courts, and the courts upheld these statutes not only in the case of foreign corporations not engaged in interstate commerce, but also in the case of those engaged in interstate commerce.

The basis for rationalization of the new jurisdiction thus given to the states has caused a great deal of trouble. There have been five main methods of explaining their jurisdiction: (a) consent; (b) submission; (c)

¹¹Collins v. Page, Style's Reports 124 (1649).

¹²Bank of Augusta v. Earle, 13 Pet. 519, 588 (1839); McQueen v. Middletown Mfg. Co., 16 Johns. 6 (1819).

doing an act which a state could forbid; (d) presence in the state; and (e) propriety and convenience. The first ground on which jurisdiction was based was that of consent." Since the state had the power to keep a foreign corporation out of the state, it could, as a condition of allowing it to come into the state, require it to consent to the appointment of an agent for the service of process, etc., but when the jurisdiction was upheld against a corporation which was engaged only in interstate commerce which the state could not prohibit, the consent theory broke down." The submission theory is a good deal like the consent theory in that it holds that when a corporation does business in the state it submits to certain reasonable laws regarding jurisdiction and it encounters the same difficulty as the consent theory. The theory that doing an act which the state could forbid subjects the corporation to the state's jurisdiction has been championed by a magazine writer but has not found support in the cases." It means that if one does an act or causes an event within the state which, under the laws of the state at that time, subjects him to jurisdiction, that is a sufficient basis. The theory of presence in the state is probably the strongest theory upon which a state's jurisdiction over foreign corporations can be made to rest." When is a corporation present in the state? It has generally been said that when it is doing business in the state. But when is a corporation doing business in a state? Perhaps a safe

"*Lafayette Insurance Company v. French*, 18 How. 404 (1853); *St. Clair v. Cox*, 106 U. S. 350 (1882).

"*International Harvester Co. v. Kentucky*, 234 U. S. 579 (1914).

"*Scott, Jurisdiction Over Non-Resident Motorists*, 39 HARV. L. REV. 563 (1926).

"*International Harvester Co. v. Kentucky*, 234 U. S. 579 (1914); *Cannon Mfg. Co. v. Cudahay Co.*, 267 U. S. 333 (1924).

test would be that it is doing business in a state whenever it does permanent or continuous acts which constitute some substantial part of its ordinary and principal business. Stimson has suggested as a test for the presence theory a very practical and simple test. According to his test a state would have jurisdiction over a foreign corporation whenever one or more of its agents or servants, acting in its behalf, is within the territory of the state."^a The adoption of the presence theory did not, however, mean the discarding of the consent theory."^b The explanation of propriety and convenience is the civil law rule which gives that court or state jurisdiction which ought to exercise it, and there is some indication that Anglo-American law is tending towards the civil law position."^c Hence, now on one theory or another, foreign corporations are subjected to suits in the courts of any state as much as natural persons, except in the case of transitory causes of action involving foreign corporations engaged in interstate commerce.

The Judiciary Act of 1789, in giving effect to the diverse citizenship clause, limited suits brought in the circuit courts to districts wherein the defendant was an inhabitant or could be found. While the old classical theory obtained that a corporation could have no existence beyond the territorial limits of the state of its origin, it followed that a corporation could not be an

^aStimson, *Jurisdiction Over Foreign Corporations*, 18 ST. LOUIS L. REV. 195 (1933).

^b*Simon v. Southern Ry.*, 236 U. S. 115 (1914); *Pennsylvania Fire Ins. Co. v. Gold Issue Mining and Milling Co.*, 243 U. S. 93 (1916); *L. & N. Ry. Co. v. Chatters*, 279 U. S. 320 (1929).

^c*Hess v. Pawloski*, 274 U. S. 352 (1927); *Davidson v. Daugherty*, 241 N. W. 700 (Iowa, 1931); Ross, *The Shifting Basis of Jurisdiction*, 17 MINN. L. REV. 146 (1933).

inhabitant or found in other states. Thus, corporations were able to evade suits in federal courts, even in states, where they carried on business. This early position was later circumvented by the doctrine of consent where a state provided by statute for the appointment of an agent to accept service as a condition precedent to doing business, and later where two states had no such statute on the theory that the corporation was found in any state wherein it did business. Finally, the Judicature Act was amended in 1887 by omitting the words "in which he shall be found" thus leaving federal jurisdiction for diverse citizenship to suits brought in the district whereof either the plaintiff or the defendant was an inhabitant. Since it is held that a corporation is an inhabitant of only the state of its origin, it follows that today a corporation may be sued in the federal courts of its chartering state only by non-residents, and in the federal courts of other states if doing business therein, by residents."

At the present time it is popular for most corporations to incorporate in Delaware, New Jersey, and a few other favorite states. Why is this? Because those states, especially Delaware, have lax corporation laws such as the corporations want but the people generally do not want corporations to have. Delaware has these laws because it brings corporations to it and corporations bring revenue. In other words, Delaware is working this racket on the other states because of the money the corporations pay her for doing so. She now gets four or five millions a year from initial incorporation fees and annual franchise taxes, and it has been suggested that she could obtain enough revenue so that she could abolish all other taxes. The laws which she gives

"79 U. OF PA. L. REV. 965 (1931); 11 TEX. L. REV. 359 (1933).

corporations in exchange for this revenue permit: (a) directors not to be stockholders; (b) officers and directors not to reside in the state; (c) directors' meetings to be held outside the state but not stockholders' meetings (who therefore never attend meetings); (d) directors to issue new stock without the approval of the stockholders; (e) the election of directors to be by a limited class of stockholders; (f) issuance of stock for property, services, rights, and the products of one's brain; (g) issuance of stock without par value; (h) issuance of stock purchase warrants (whereby directors may gamble without risk); (i) a majority of the board to constitute a quorum; (j) Wilmington trust companies to furnish office boy incorporators."

In this way, other states not only lose their share of the revenue which Delaware gets, but they have turned loose to prey upon them a flood of piratically organized corporations out to fleece other states, the public, their own stockholders and anyone not a director. No wonder the states in turn try to prey upon such corporations by tax and police power laws. If the corporations are to be protected against the states, the states must also be protected against the corporations, and it is believed the states and federal government have a ready weapon available to break up the game of racketeering of Delaware and all other states like her, and that is federal incorporation of all corporations engaged in interstate commerce and state reincorporation of all other foreign corporations."

LIABILITY: 3. DOMESTIC CORPORATIONS

Just as domestic corporations are protected by the

**150 Atlantic Monthly 268.

****Supra* note 82.

Constitution, so far as concerns property, to the same, and, in the case of contracts, to a greater extent, than natural persons; so they also in general have the same liabilities as natural persons. They are subject to the same powers of taxation, the same power of eminent domain, and the same police power. The cases heretofore cited are sufficient authority for this general proposition." A few special applications of the police power will be adverted to.

It is not unconstitutional as impairing the obligation of contracts made by a corporation with third parties to dissolve a corporation whether or not a power to repeal has been reserved," provided creditors are not deprived of the right to resort to the property of the corporation," but it would impair the contract between the corporation and the state to dissolve a corporation unless there is some act or neglect constituting a cause for forfeiture or the power to repeal has been reserved." As to whether it is constitutional for a state to authorize a majority of the stockholders of a corporation to amend its charter so as to issue no par stock in lieu of existing stock, or to change voting powers of stockholders, or to authorize it to engage in a new business, or to merge with another corporation, there is a conflict in the decisions, but the better view is that this is not an impairment of the contract between the corporation and dissenting stockholders even where the power to annul has not been reserved if the corporation, if not a public utility, is required to buy the stock of such dissenting stockholders at full value if they so elect; and

^{**}*Supra* notes 6, 40.

^{**}*Mumma v. Potomac Co.*, 8 Pet. 281 (1834).

^{**}*Lothrop v. Stedman*, 42 Conn. 584 (1875); *Commonwealth v. Essex Co.*, 13 Gray 239 (1859).

^{**}*Dartmouth College v. Woodward*, 4 Wheat. 518 (1819).

this view has abundant support if the power to annul has been reserved.¹⁰⁰ The basis for this rule in all cases is that such action is a proper exercise of the police power to which all contracts are generally subject.

In some states constitutional prohibitions now forbid the creation of corporations by special acts, or the conferring of corporate powers by such acts, though in the absence of such prohibitions corporations may still be created by special acts,¹⁰¹ but even under such provisions it is constitutional for a legislature to change the name of a corporation by special act, unless general laws otherwise provide.¹⁰²

The enactment of statutes providing for the inspection of the books and other records of a corporation at reasonable times by the stockholders and creditors is a proper exercise of the police power and does not impair the obligation of any contract or deprive the corporation of its property without due process of law.¹⁰³

It is due process of law to punish a corporation for contempt to the same extent as a natural person, and the fact that an officer of the corporation through whom the contempt was committed may also be punished is no defense. This power exists independently of statute and cannot be curtailed by statute since it would be

¹⁰⁰*Canada So. R. Co. v. Gebhard*, 109 U. S. 527 (1883); *Hale v. Cheshire R. Co.*, 161 Mass. 443, 37 N. E. 307 (1893); *Market St. R. Co. v. Hellman*, 109 Cal. 571, 42 Pac. 225 (1895); *McKee v. Chautauqua Assembly*, 130 Fed. 536 (C. C. A. 2nd, 1904); *Colby v. Equitable Trust Co.*, 108 N. Y. S. 978 (1908); *Winfrey v. Riverside Cotton Mills*, 113 Va. 717, 75 S. E. 305 (1912); *Randle v. Winona Coal Co.*, 206 Ala. 254, 89 So. 790 (1921).

¹⁰¹*Oregon Ry. & N. Co. v. Oregonian Ry. Co.*, 130 U. S. 1 (1888); *School District, No. 36 v. St. Joseph F. & M. I. Co.*, 103 U. S. 707 (1880).

¹⁰²*Wallace v. Loomis*, 97 U. S. 146 (1877); *Hazellett v. Butler University*, 84 Ind. 230 (1882).

¹⁰³*Venner v. Chicago City Ry. Co.*, 246 Ill. 170, 92 N. E. 643 (1910); *Schmidt v. Anderson*, 29 N. D. 262, 150 N. W. 871 (1915).

a violation of the doctrine of separation of powers.¹⁰⁴

Stockholders may be held liable to pay any balance on unpaid stock, though they, in addition, are under a statutory liability imposed at the time of the creation of the corporation and to refund dividends paid them where the corporation is insolvent.¹⁰⁵

It is due process of law to punish corporations for many crimes and the whole modern tendency of the law is to subject corporations, as nearly as may be, to the same criminal law as individuals.¹⁰⁶ Prima facie the word person in a penal statute includes corporations.¹⁰⁷ Congress has power, under the Interstate Commerce Clause, to regulate corporations as it has done in the Sherman Act and the Clayton Act, and it has no contract clause limiting its power, but only the due process clause.¹⁰⁸

Blue sky laws can be passed by the states without interfering with interstate commerce or violating the equality or due process clauses.¹⁰⁹

Public utility companies can, under the due process clause, be subjected to the social control, called the law of public callings,¹¹⁰ and may be regulated by public service commissions without violating the doctrine of

¹⁰⁴*Fielder v. Bambrick Bros. Construction Co.*, 162 Mo. App. 528, 142 S. W. 1111 (1912); *Consolidated Rendering Co. v. Vermont*, 207 U. S. 541 (1908); *Merchants' Stock & Gas Co. v. Board of Trade*, 201 Fed. 20 (C. C. A. 8th, 1912); *Same*, 223 U. S. 639 (1912).

¹⁰⁵*Randall Printing Co. v. Sanitas Mineral Water Co.*, 120 Minn. 268, 139 N. W. 606 (1913); *Finn v. Brown*, 142 U. S. 56 (1891).

¹⁰⁶*Joplin Mercantile Co. v. United States*, 213 Fed. 926 (C. C. A. 8th, 1914); *Southern Express Co. v. State*, 1 Ga. App. 700, 58 S. E. 67 (1907).

¹⁰⁷*Overland Cotton Mill Co. v. People*, 32 Colo. 263, 75 Pac. 924 (1907).

¹⁰⁸*United States v. Joint Traffic Association*, 171 U. S. 505 (1898); *Nash v. United States*, 229 U. S. 373 (1913); *United States v. United Shoe Machinery Co.*, 234 Fed. 127 (D. C. Mo., 1916).

¹⁰⁹*Hall v. Geiger-Jones Co.*, 242 U. S. 539 (1917).

¹¹⁰*Munn v. Illinois*, 94 U. S. 113 (1876).

delegation of powers or separation of powers."¹¹¹

The practice of law by corporations is illegal. A statute so prohibiting is a proper exercise of the police power and without a statute the court may declare it illegal because of the judicial power created by the doctrine of separation of powers."¹¹²

III.

In some respects it is apparent corporations have been given too much protection and too little liability. Public utility corporations, for example, have been given too much protection in the matter of their rates and their rate bases. Corporations are still given too much protection in the matter of taxation and the matter of utility franchises and rates under the contract clause. Corporations incorporated in Delaware and other states copying Delaware have been given too many advantages. There has not been enough federal taxation of interstate commerce. Perhaps corporations also should be subject to greater income taxes and to more price fixing. But on the whole what is wanted is not so much new law as better application of our present laws. Some of the old law has already been sufficiently reformed. There is need outside of a few states for little further reformation. What then should be the changes in the future in the social control of corporations? For the most part the social control of the future must have a change in objective.

¹¹¹*Louisville & N. R. Co. v. Garrett*, 231 U. S. 298 (1913).

¹¹²*Meisel & Co. v. National Jewelers' Board of Trade*, 152 N. Y. S. 913 (1915); *In re Co-operative Law Co.*, 198 N. Y. 479, 92 N. E. 15 (1910). The practice of dentistry by corporations may also be prohibited in the exercise of the police power. *Painless Parker v. Board of Dental Examiners*, 84 Cal. Dec. 223 (1932). But the exercise of the police power in this type of cases seems to be limited to the learned professions. 21 CALIF. L. REV. 279 (1933).

The old viewpoint with regard to corporations was that the owners of the property should be protected, and that those in control were merely trustees for such owners. Some contend that this should be the future reform of our corporations, but with the wide dispersion of ownership in many corporations the owners now have become so inactive and irresponsible that this reform is not feasible.

Another view which might be taken would be to protect those in control, which is our present plan. The only result of this system of corporate management is corporate plundering. Whatever might is able to do is made right.

A third view and the one which should be taken is that corporations must serve society. Wages and security must be given by them to their employees; services must be given to the public and stabilization must be given to business. People must realize that the corporation is one form of social organization. It is a dominant institution of our modern world, but it must be controlled for the common good. Economic power can now compete on even terms with political power. In the future either the corporation must be dominated by the state or the state must become the corporation.